

**Estimating System Deficiencies
Found During Audit
of Proposed Fiscal Year 2003
Forward Pricing Labor Rates**

April 2003

Reference Number: 2003-1C-087

This report has cleared the Treasury Inspector General for Tax Administration disclosure review process and information determined to be restricted from public release has been redacted from this document.



INSPECTOR GENERAL
for TAX
ADMINISTRATION

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

April 21, 2003

MEMORANDUM FOR DAVID A. GRANT
DIRECTOR OF PROCUREMENT
INTERNAL REVENUE SERVICE

FROM: Daniel R. Devlin
Assistant Inspector General for Audit (Headquarters Operations
and Exempt Organizations Programs)

SUBJECT: Estimating System Deficiencies Found During Audit of Proposed
Fiscal Year 2003 Forward Pricing Labor Rates
(Audit #200310002.029)

The Defense Contract Audit Agency (DCAA) audited a certain contractor's Civil Division estimating practices used in preparing its proposed direct labor forward pricing rate and full-time accounting factor proposals dated August 21, 2002. The proposals were effective July 6, 2002, through June 30, 2003. The purpose of this audit was to determine if the contractor consistently complied with established estimating system internal controls for developing accurate, current, and complete cost estimates.

The DCAA opined that certain estimating practices used by the contractor in preparing the forward pricing direct labor rates proposed for July 6, 2002, through June 30, 2003, require corrective action to improve the reliability of its future direct labor rate estimates. The DCAA noted that the contractor is lacking adequate policies and procedures for calculating direct labor forward pricing rates and adequate policies and procedures for inclusion of all Civil Division employees for forward pricing direct labor rate purposes and calculations. Due to the number and significance of the variances in labor category rates, the DCAA concluded that using only annual escalation rates to project direct labor rates for future years is not appropriate and may result in over- or under-bidding labor rates for Federal Government contract purposes. In addition, the contractor's practice of excluding certain employees for forward pricing labor rate development is an estimating deficiency that may also lead to over- or under-bidding on Federal Government contracts.

The DCAA was unable to estimate the magnitude of the total potential cost impact of the estimating system deficiencies; however, approximately \$2.4 billion in proposals were submitted by the Civil Division to the Federal Government during Fiscal Year 2002. The DCAA recommends that the contractor's Civil Division develop adequate written policies and procedures for calculating direct labor forward pricing rates.

The information in this report should not be used for purposes other than that intended without prior consultation with the Treasury Inspector General for Tax Administration regarding its applicability.

If you have any questions, please contact me at (202) 622-8500 or John R. Wright, Director at (202) 927-7077.

Attachment

NOTICE:

The Office of Inspector General for Tax Administration has no objection to the release of this report, at the discretion of the contracting officer, to duly authorized representatives of the contractor.

The contractor information contained in this report is proprietary information. The restrictions of 18 USC 1905 must be followed in releasing any information to the public.

This report may not be released without the approval of this office, except to an agency requesting the report for use in negotiating or administering a contract with the contractor.

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